Independent Review of Bangladesh's Development

বাংলাদেশের উন্নয়নের স্বাধীন পর্যালোচনা

State of the Bangladesh Economy in FY2019-20

First Reading

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CENTRE FOR POLICY DIALOGUE

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The CPD IRBD 2019 Team alone remains responsible for the analyses, interpretations and conclusions presented in this report.

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Section I. Introduction

Context of the Presentation

- To track the progress of the post-budget first quarter (Q1 of FY20)
- Closure of the 7th FYP (2020)
- End of first full year of the new elected government (2019)
- Follow-up on the electoral pledges

Objective of the Presentation

- To identify the key areas demanding urgent attention, based on early signals for successful implementation of the budget for FY20

Scope of the Presentation

CPD raises red flag in four areas where immediate attention is required:

1. Revenue Mobilisation
2. Banking Sector
3. Capital Market
4. External Sector Performance

Section II. The Revenue Challenge

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2. The Revenue Challenge

No major breakthrough in revenue mobilisation!

- Revenue-GDP ratio has been decelerating since FY2012
- In FY19, total revenue-GDP ratio of Bangladesh was only 9.9% with the tax-GDP ratio being 8.9% (provisional figures)
  - Average tax-GDP ratio in developing countries (UN classification) is about 15% in 2017
  - The 7FYP aims to reach total revenue-GDP and tax-GDP ratio of 16.1% and 14.1% respectively by FY20
    - This appears to be a far cry, notwithstanding high imputed GDP growth rate
  - The Public Finance Management (PFM) Action Plan 2018-23 now aims to raise tax-GDP ratio further, from the 14.1% by 2023 – less ambitious!
    - Surprisingly, this is below the developing country average of 15%
    - Also, the target of 14.1% is set to be achieved by 2023 – three years later than the targeted timeframe of 7FYP
    - Perhaps a more '*pragmatic*' approach given the current situation

Revenue mobilisation could not keep pace with GDP growth!

- During FY10-14, total revenue increased by 1.2% for 1% growth in GDP. However, during FY15-19, total revenue increased by 1.1% for 1% growth in GDP – indicating a fall in elasticity
- During FY10-14, income tax collection rose by 1.9% for 1% increase in GDP whereas, during FY15-19, income tax collection growth came down to 1.0% for 1% growth in GDP
- On the other hand, growth in indirect tax (such as VAT and SD) showed rather optimistic trend with respect to GDP growth for the aforesaid two periods
    - Rising inequity in the tax system!?

Elasticity with respect to GDP

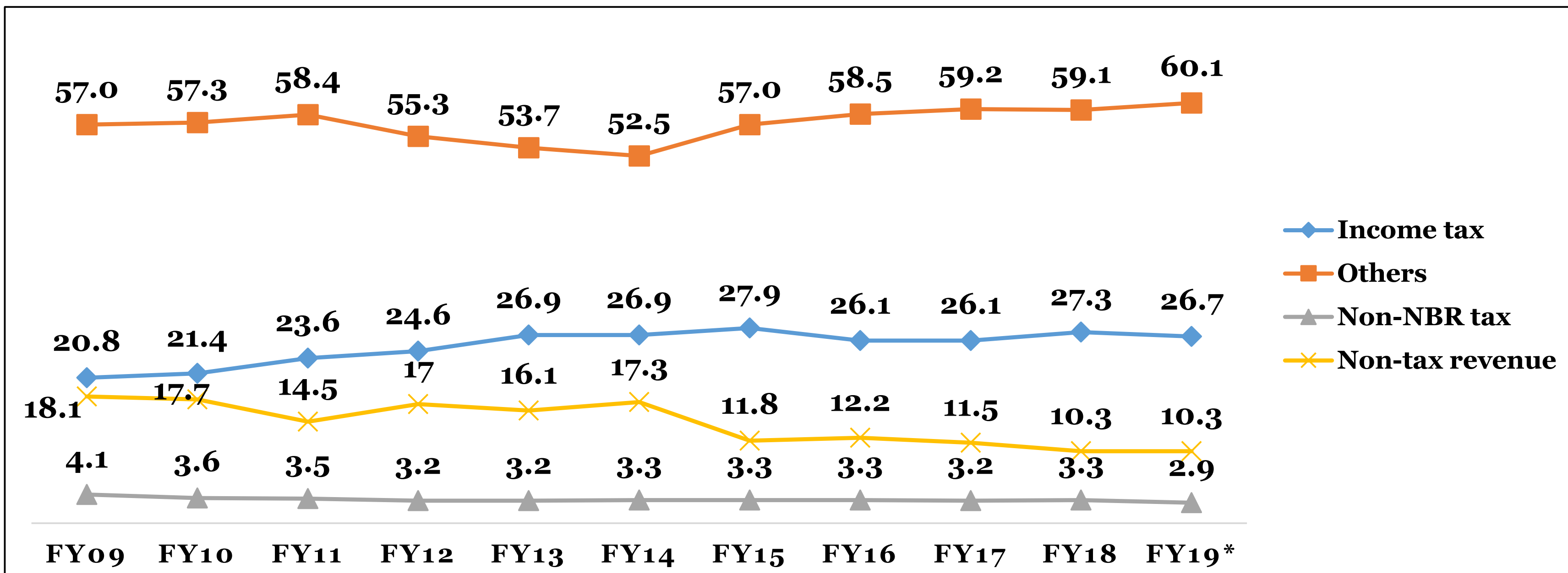
Source	FY10 - FY14	FY15 – FY19
NBR tax	**1.3**	**1.1**
Income tax	1.9	1.0
VAT	1.1	1.3
Import duty	0.7	0.9
Excise duty	2.0	2.0
SD	1.0	1.2
Other taxes	0.8	0.4
Non-NBR tax	**1.0**	**0.8**
Total tax revenue	**1.3**	**1.1**
Non-tax revenue	**1.2**	**0.8**
Total revenue	**1.2**	**1.1**

Source: Calculated from MoF and BBS data

Revenue mobilisation is dominated by indirect tax collection with consequent distributive implications

- ❑ Income tax's share in total revenue collection exhibited increasing trend between FY09 and FY15. However, after FY15 this share has shown a declining trend
- ❑ Reliance on indirect taxes (VAT, SD, export and import duty etc.) for revenue mobilisation creates added pressure for the low- and middle-income section of the society

Sources of revenue mobilisation (in Per cent)



Source: Calculated from MoF data
Note: * indicates provisional figures

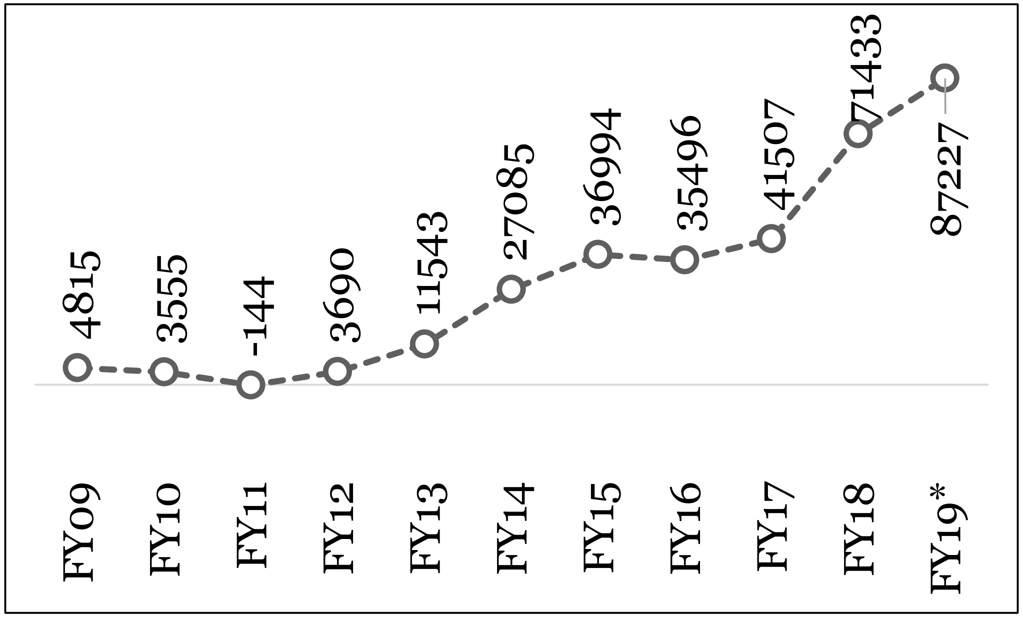
2. The Revenue Challenge

Revenue shortfall has become a major concern – limiting public services for the citizens!

- Increased to Tk.87,227 cr. in FY19 (early estimated figure) according to MoF data – about 3.4% of GDP
  - CPD's projection of Tk. 85,000 crore turns out to be regrettably close to reality

- Attainment of the shortfall in FY19 could easily:
  - Provide 4 times current health services!
  - Double the present education budget!
  - Double prevailing social protection!
  - Finance almost three more Padma bridges in a single year!

Actual revenue shortfall (in Crore Tk.)



Source: Calculated from MoF data
Note: * indicates provisional figures

Indirect taxes are mainly causing large revenue shortfall

Direct tax's share in total NBR shortfall decreased during FY15-19

- From 65.2% in FY15 to 40.5% in FY19
  - The share was increasing between FY12 and FY15
- Income tax LTU's share in total NBR shortfall appears to be decreasing - from 16.5% in FY15 to 3.8% in FY19

Indirect tax's share in total NBR shortfall increased during FY15-19

- From 34.8% in FY15 to 59.5% in FY19
  - The share was decreasing between FY12 and FY15
- VAT LTU's share in total NBR shortfall exhibits fluctuations

So direct tax targets are more pragmatic than indirect tax targets! – Impact of VAT reform, which could not be implemented in stipulated time?

2. The Revenue Challenge

Within the components of indirect tax:

Indirect tax at local stage's share in total NBR shortfall decreased during FY15-19

- From 53.4% in FY15 to 31.0% in FY19
  - Within the local stage components, share of VAT in total NBR shortfall exhibited a decreasing trend between FY15 and FY19
  - On the other hand, share of SD in total NBR shortfall exhibited fluctuations with a spike in FY19

Indirect tax at external stage's share in total NBR shortfall increased during FY15-19

- From (-)18.6% in FY15 to 28.5% in FY19
  - This is primarily driven by shortfalls in import duty and VAT collection on external stage – impact of low import growth?

Exemptions? Evasions? Or Slow economic growth?

2. The Revenue Challenge

Composition of NBR revenue shortfall (in %)

Components			FY15	FY16	FY17	FY18*	FY19*
Indirect tax	a. External	a.1 Import duty	-6.9	3.6	4.7	6.1	12.3
		a.2 VAT	-5.7	4.1	0.5	8.8	11.9
		a.3 SD	-6.0	-1.8	-0.9	4.1	4.3
		a.4 Export duty	-0.1	0.0	0.1	0.0	0.0
		Subtotal	**-18.6**	**5.9**	**4.4**	**19.0**	**28.5**
	b. Local	b.1 Excise duty	0.7	-1.6	-1.3	-0.7	-0.1
		b.2 VAT	46.3	25.8	30.3	25.9	15.3
		b.3 SD	6.4	10.2	4.5	1.7	15.7
		b.4 Turnover tax	0.0	0.0	0.0	0.0	0.0
		Subtotal	**53.4**	**34.4**	**33.5**	**26.8**	**31.0**
	Total indirect tax (a+b)		**34.8**	**40.3**	**37.9**	**45.8**	**59.5**
Direct tax	c. Income tax		64.9	58.8	61.0	54.0	40.0
	d. Travel tax		0.3	0.9	1.1	0.1	0.5
	Total direct tax (c+d)		**65.2**	**59.7**	**62.1**	**54.2**	**40.5**
Grand total (a+b+c+d)			**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Calculated from NBR data

Note: * indicates provisional figures

Revenue collection scenario in the first quarter of FY20 does not appear too promising

- NBR revenue collection figures for Jul-Sep period (Q1) of FY20 reveal that nearly 84% of the shortfall is originated from indirect taxes

Source	Growth (%)				Shortfall Q1 FY20	
	Target FY20	Achieved Q1 FY19	Achieved Q1 FY20	Required Oct-Jun FY20	Crore Tk.	Share (%)
Duties at import and export stage	45.7	8.0	-1.3	60.5	6106.7	41.0
VAT at local stage	34.3	-0.9	-0.9	43.1	6429.2	43.1
Income and travel tax	58.6	14.1	11.6	69.2	2371.0	15.9
Total NBR revenue	45.4	6.1	2.6	56.6	14906.8	100.0

- Growth of duties at import and export stages was negative (-)1.3% during Jul-Sep of FY20 (8.0% in the corresponding period of FY19)
- VAT collection at local stage decreased by (-)0.9% during Jul-Sep of FY20. During the same period of FY19, this growth was also (-)0.9%
- Income tax collection increased by 11.6% during Jul-Sep of FY20 (14.1% during Jul-Sep of FY19)

Implications for Macroeconomic Management

- ***Possibility of a higher revenue collection shortfall in FY2020***
  - NBR is the single largest contributor of government exchequer (about 87%)
  - Growth of NBR revenue collection in Q1 is one of the lowest in the decade - one may expect an even higher revenue shortfall
- ***Higher revenue shortfall may lead to higher deficit-GDP ratio***
  - Lower revenue and apparently higher expenditure led to higher budget deficit
  - As per Bangladesh Bank data, the overall deficit recorded a 73.1% growth (additional about Tk. 14,194 crore) during Jul-Aug of FY20 – already 23.8% of annual target
  - Net borrowings from banking sources registered **311% growth** (additional about Tk. 18,555 crore) – already 53.8% of the annual target
  - Net sale of NSD certificates was Tk. 5,398 crore lower than that of the corresponding figure of FY19!

Implications for Macroeconomic Management

- ***Increased pressure on deficit financing in meeting the public expenditure demands***
  - As per IMED data, 4.6% of total ADP could be spent during Jul-Aug of FY20 – marginally better from the previous fiscal year (3.1% in Jul-Aug FY19)
    - Regrettably, utilisation of PA (3.1%) was one of the lowest since FY12
  - MoF data during last five fiscal years (FY13-FY18) suggests, ADP financing from revenue surplus was about 12% on an average, which declined to 7.6% in FY18
    - This prompted financing the remaining ADP expenditure needs from domestic (69%) and foreign (23%) borrowings in FY18 leading to one of the highest deficit-GDP ratio (4.7%) in recent times
    - *With the present trend, in FY20 one may not except any significant contribution from revenue surplus for financing ADP*

Implications for Macroeconomic Management

- ***Possible crowding-out effect on the private sector***
  - Net government credit registered a 34.9% growth during Jul-Aug of FY20 (highest since FY12)
  - Private sector credit registered the **slowest growth (around 10%) since FY14** during Jul-Aug period of FY20
  - Liquidity position in the money market is also not very flexible
  - Growing pressure on government's bank borrowing may leave contracted space for private investment financing

Not a pleasing outlook for private investment!

Key Challenges and Outlook

- ***Take concrete and more visible actions to broaden the tax net***
  - It is totally inexplicable why inspite of so many visible signals broadening of tax net issue is not addressed adequately
  - Currently, about 58% of total e-TIN holders (about 38 lakh) submit income tax returns. A CPD estimate (2016) based on HIES 2010 suggests, there are about **70 lakh potential taxpayers** in Bangladesh
  - NBR intends to bring 1 crore people under the tax net. As per newspaper sources, tax officials have conducted a survey and identified about 12 lakh TIN holders eligible for paying income taxes
  - According to a CPD Study, about **68% of eligible tax payers** in the country do not pay any income tax

Key Challenges and Outlook

- ***Take concrete and more visible actions to broaden the tax net***

NBR should make list of effective taxpayers public!

- Using the **e-TIN database**, the NBR could identify and pursue
  - individuals who are registered in the system but are not submitting returns; and
  - individuals who are registered, submitting returns, but are not effectively paying taxes

Key Challenges and Outlook

- ***Accelerate the pace of implementing the decentralisation plan of NBR***
  - NBR has a plan to set up tax offices in every upazilla in Bangladesh. The number of Tax Zones is planned to be increased to 63 from current 31
    - No visible progress has been made till now in implementing the plan of decentralisation of the tax offices

NBR should make visible and faster progress in implementing its decentralisation plan

Key Challenges and Outlook

- ***Do away with the practice of providing tax exemption and waivers on ad-hoc basis***
  - As per NBR data, tax revenue of about Tk. 18,700 crore was lost in FY19 due to exemptions offered in different forms. This was equivalent to **8.4% of total tax revenue** collected by NBR in FY19
    - As per early signals NBR is expected lose much larger amount of revenue in FY20 due to the broader array of exemptions in income tax and VAT, waivers, rebates, deduction of source tax on exports at pre-budget level and withdrawals of advanced tax (AT) on imports through different SROs, general orders and notifications

Ad-hoc provisions of tax exemptions reduces the revenue collection predictability. Revenue forgone for tax exemption should be calculated annually, be rationalised and if possible be reduced

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Key Challenges and Outlook

- ***Ensure smooth implementation of the VAT and SD Act 2012***

a. Incentivise business entities to register through VAT online system

- As per the guideline of VAT-online system and upon detecting furnished fake information by around 60% of e-BIN holders in their VAT registration form, NBR directed all e-BIN holders (**166,000**) to update their VAT registration information to 13-digit BINs by July 31, 2019
- Very poor response prompted NBR to extend the deadline till 14 Aug'19
- Only about **22% businesses** obtained as of September 30, 2019
- Apparently, up to end October 2019, **only 42% have registered** – deadline extended to 30 Nov'19
- Large companies with backward linkage manufacturing units are facing **complexities in obtaining central BINs** due to the existence of term 'identical and similar' which was not present in the VAT law-1991

NBR should eliminate all the hurdles with regard to registration and getting updated BINs and central BINs

Key Challenges and Outlook

- ***Ensure smooth implementation of the VAT and SD Act 2012***

b. Guarantee early procurement and installation of electronic devices to curb VAT evasion

- The new VAT law has made it mandatory for the shop owners and business entities to keep records of VAT challan through Electronic Fiscal Device (EFD) and Sales Data Controller (SDC)
  - Initially, the NBR planned to install the devices at stores by November 2018, but it could not complete its own preparations
  - NBR placed a work order to procure 100,000 EFDs along with delivering the first 10,000 EFDs to the business entities within August 2019. However, as of end October 2019, the first instalment of EFDs could not be implemented

NBR should gear up pace of procurement and installation of devices which is mandatory for all outlets with the annual turnover exceeding Tk. 50 lakh a year

Key Challenges and Outlook

- ***Ensure smooth implementation of the VAT and SD Act 2012***

c. Ensure hassle free submission of VAT returns

- NBR introduced the online VAT return system in April 2019. Businesses have been instructed to submit their return using the online VAT system under the new VAT law
  - However, **none of the new 13-digit BIN holders** could submit their return online as of October 15, 2019
  - The large taxpayers have failed to submit their return due to non-availability of the VAT return form (VAT 9.1 form) and relevant documents on the VAT online system, problem in obtaining the 13-digit BIN needed to file the online VAT returns, differences in supplementary duties between VAT law and online system and complexities in accessing the online system (Financial Express, 2019)

NBR should take necessary measures on an urget basis to solve the technical errors and complexities regarding accessing and submitting the returns through online server

Key Challenges and Outlook

- ***Stop black money whitening scope and bring the tax evaders on board***
  - The existing black money whitening facility through voluntary disclosure of undisclosed income failed to register the expected response – apparently only **Tk. 196 crore** could be legalised from 220 people during FY17-FY19 period
  - Breakthrough in curbing tax evasion is yet to be visible

NBR should make it clear and transparent how it will be benefited from the recent drives concerning the 'casino economics'

Section III. Banking Sector

Stuck in a Quagmire of Woes

3. Banking Sector
Stuck in a Quagmire of Woes

- While Bangladesh is known for being one of the fastest growing economies in the world, its **banking sector is in the grip of despair**.

- All major parameters of the banking sector indicate its persistent fragility with no signs of revival on the horizon.

- Reforms in the banking sector are also not in sight anytime soon as the sector grapples with huge governance crisis.

- During the recent past, the difficulties of the banking sector have been exacerbated by the following **symptoms**:
  - *Drop in private sector credit growth*
  - *Mounting liquidity stress*
  - *Unsuccessful cap on interest rates*
  - *Unabated non-performing loans (NPLs)*
  - *Massive loan rescheduling and writing-off*
  - *Worrying capital inadequacy in certain banks*
  - *Futile recapitalisation of banks*

Credit growth falling short of targets - supply side problem?

- ***Domestic credit growth*** has been **stagnant** at 13.46% in August 2019. It was 13.23% in August 2018.
  - Domestic credit growth of 13.46% is below the target of 14.5% set out in the Monetary Policy Statement (MPS) of FY2020.
- ***Private sector credit growth*** has **decreased significantly** from 14.94% in August 2018 to 10.68% in August 2019.
  - Private sector credit growth (10.68%) is also below the target of 13.2% set out in the MPS of FY2020.

Figure: Domestic Credit Growth, Target vs Actual (in %)

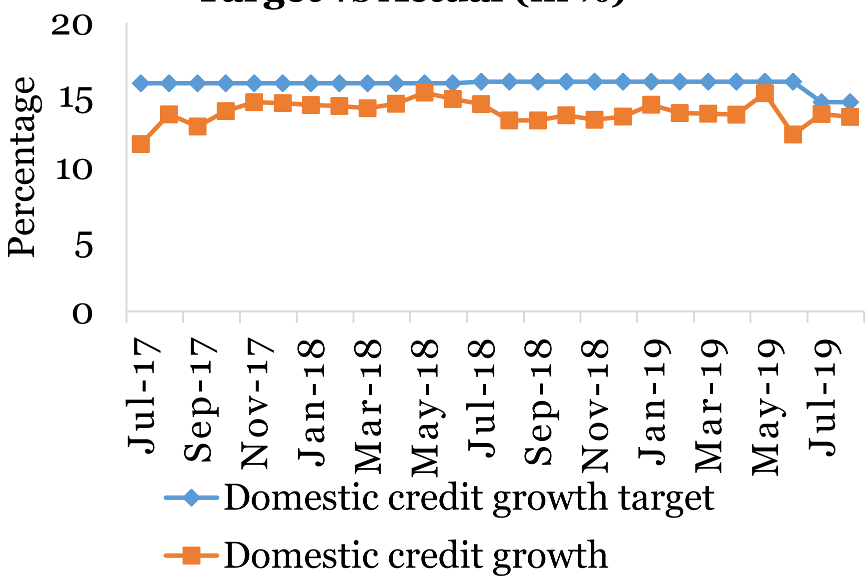
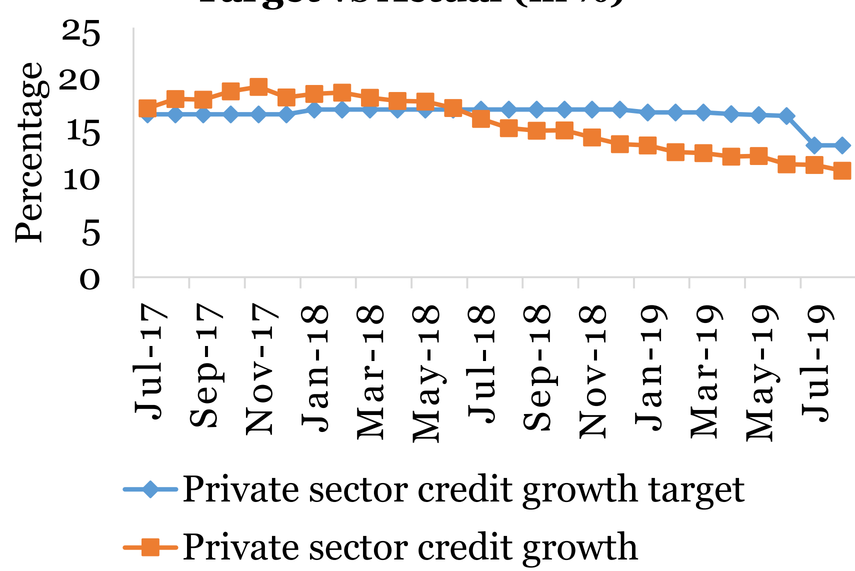


Figure: Private Sector Credit Growth, Target vs Actual (in %)



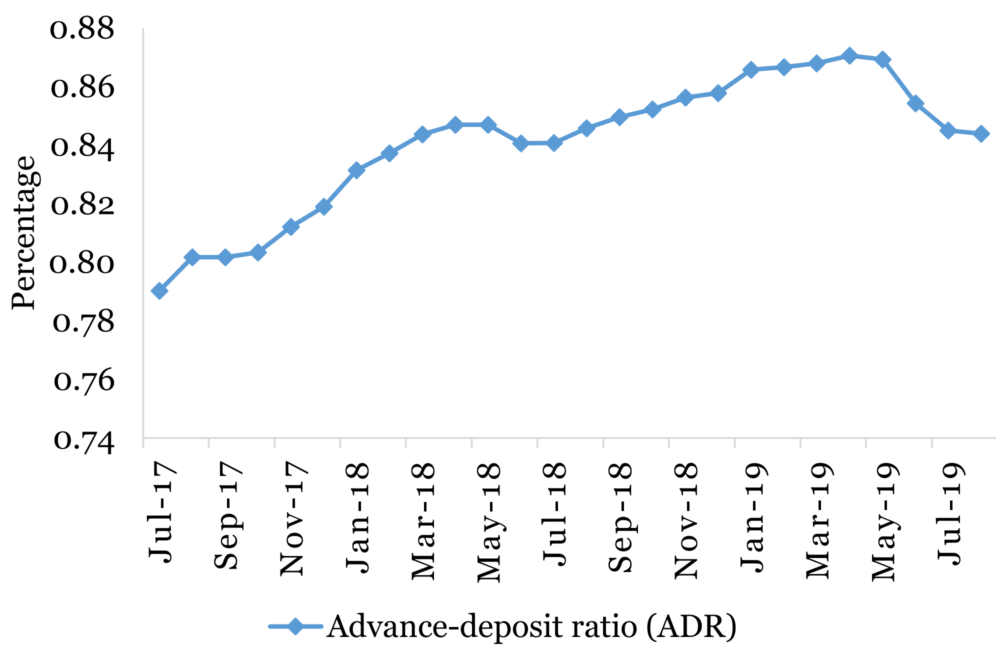
3. Banking Sector
Stuck in a Quagmire of Woes

Credit growth falling short of targets - supply side problem?

- In view of the weak growth of credit, Bangladesh Bank revised the credit targets in the MPS for FY 2020 downwards from the targets of MPS for January-June 2019 for both public and private sectors.
- Weak growth in private sector credit is due to slow growth of bank deposits and directives to banks by Bangladesh Bank to maintain a lending rate at 9%.

- Banks have struggled to keep Advance-Deposit Ratio (ADR) below the threshold of 85%, as recommended by Bangladesh Bank.
- ADR of banks declined during July - August 2019.
- **This indicates that industrial activity and investment are yet to pick up.**
- This could hamper the growth prospects of the economy.

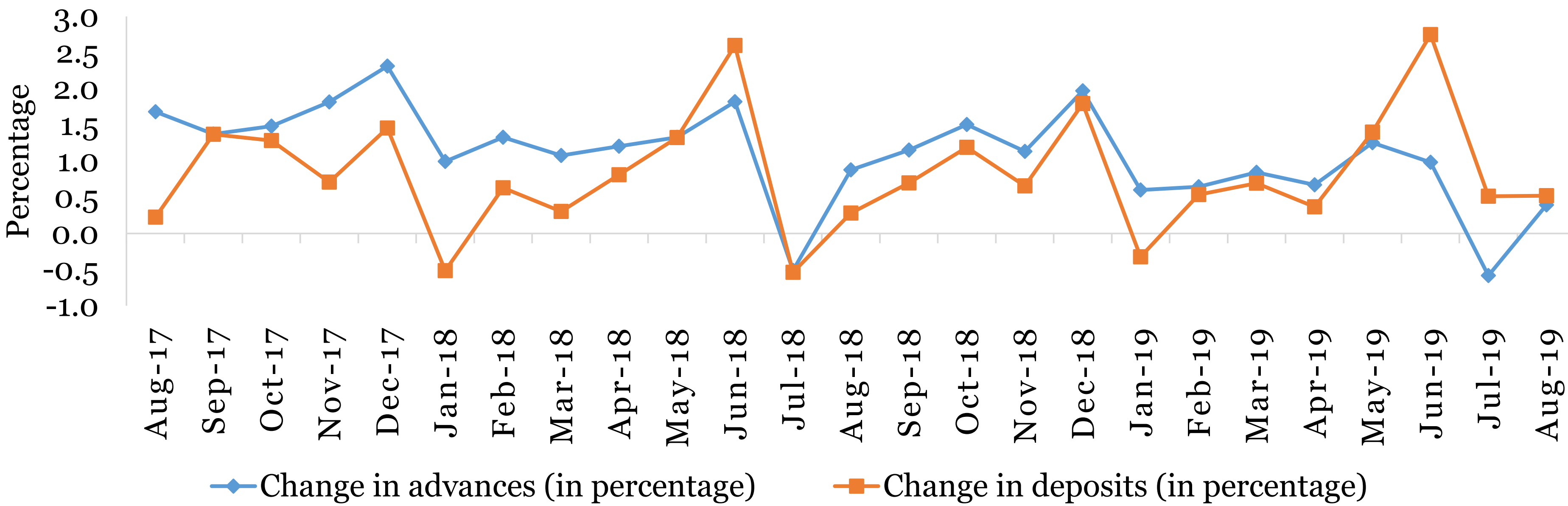
Figure: Advance-deposit ratio



Mounting liquidity stress runs the risk of economic downturn

- Though credit growth has fallen, liquidity stress in banks has mounted. This is due to lower growth of deposits compared to advances during the period from August 2017 to August 2019.
- Over the last two years, the **average growth rate of advances was 1.12%,** whilst the **average growth rate of deposits was 0.84%.**
- In fact, during this 24-month period, the growth rate of advances was always greater than the growth rate of deposits, except in four months: July 2018 and May-August 2019.

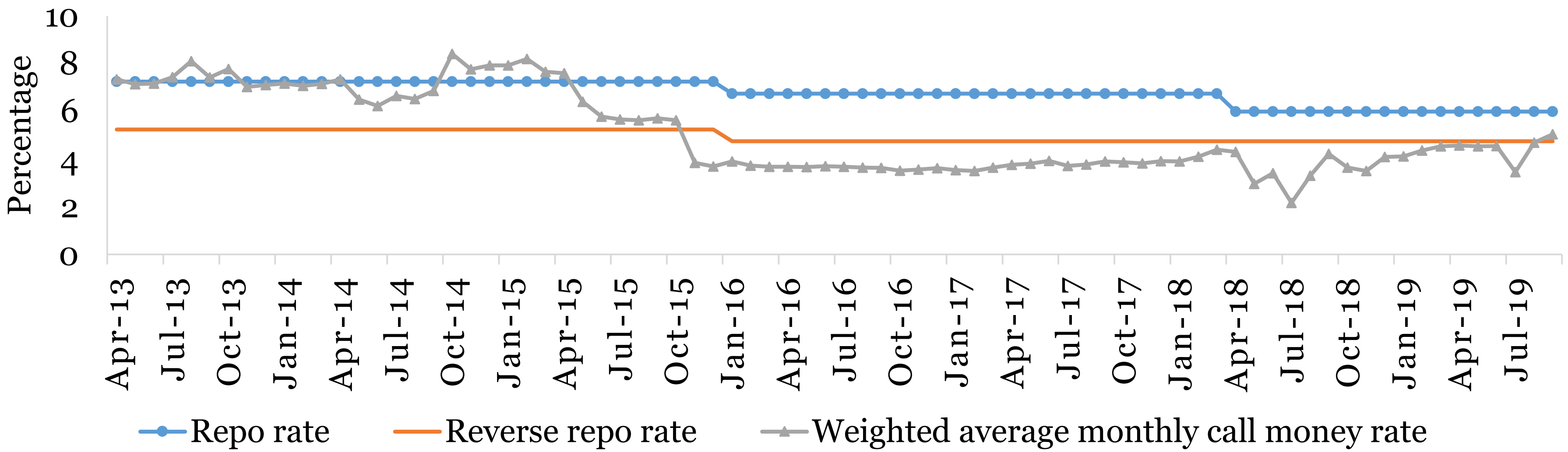
Figure: Growth of advances and deposits (in percentage)



Mounting liquidity stress runs the risk of economic downturn

- Liquidity pressure in the banking sector was also evident through the increasing trend of call money rates.
- The weighted average monthly call money rate increased from 2.17% in July 2018 to 5.04% in September 2019, which was the highest since October 2015.
- This implies that the **demand for cash**, particularly by **under-capitalised banks**, has been **high**.

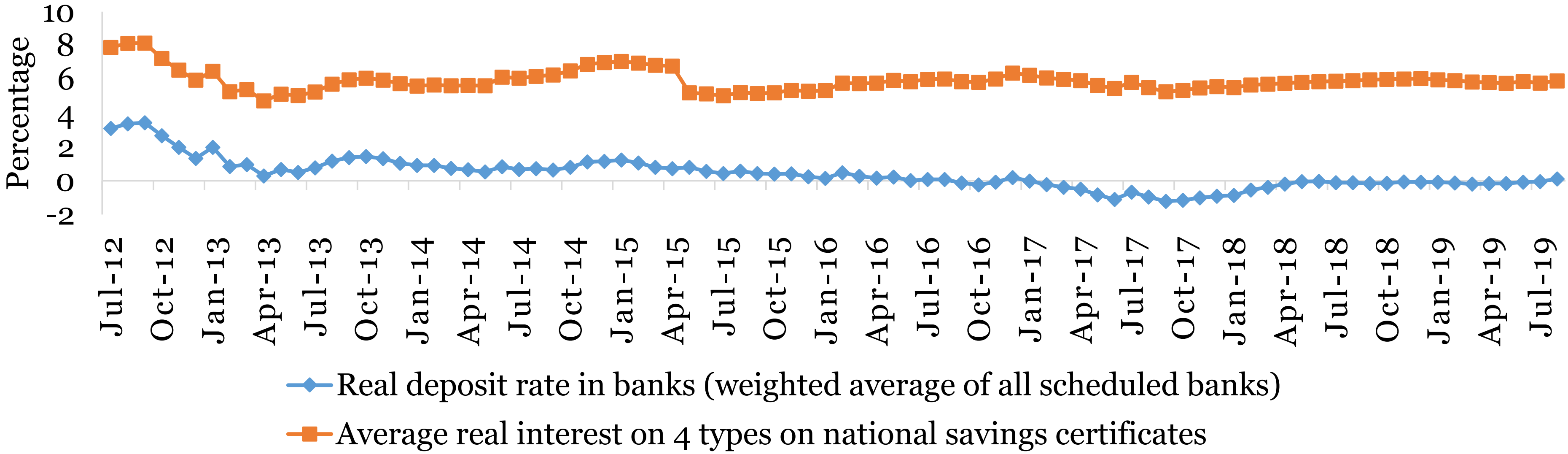
Figure: Repo, reverse repo and call money rates (in %)



Mounting liquidity stress runs the risk of economic downturn

- Difference in real interest rates of bank deposits and National Savings Certificates (NSCs) has also contributed to liquidity pressure in banks.
- In August 2019, *the real weighted average deposit rate* in commercial banks was 0.11% and *the average real interest rate on four types of NSCs* was 5.91%.
- In fact, during the period from July 2012 to July 2019, the difference between *the average real interest rate* on NSCs and *the average real interest rate* on bank deposits was 5.53%.
- Research conducted by Bangladesh Bank has shown that a 1 percentage point increase in the gap between real NSC rate and real bank deposit rate decreases the overall liquidity in the banking sector by 0.24 percentage points.

Figure: Average real interest rate on NSCs and average real interest rate on bank deposits (%)

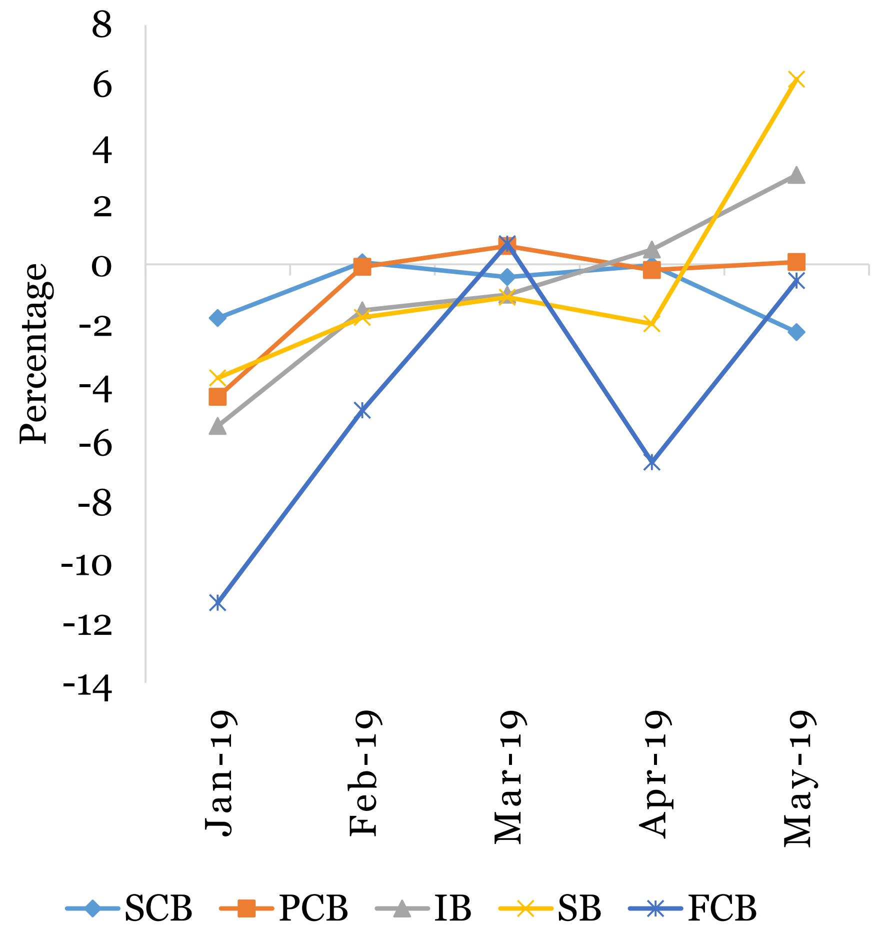


CPD (2019): State of the Bangladesh Economy in FY2019-20 (First Reading)

Mounting liquidity stress runs the risk of economic downturn

- The weak deposit growth is due to a host of factors:
  - **nearly zero or below zero real interest rate on deposits**
  - cap on deposit rate at 6%
  - relatively higher interest rates offered on NSCs
  - falling confidence of depositors due to **high NPLs**
  - **illicit financial outflows**.
- If liquidity crisis persists, private sector credit growth will further slow down and the economy will run the **risk of a downturn**.

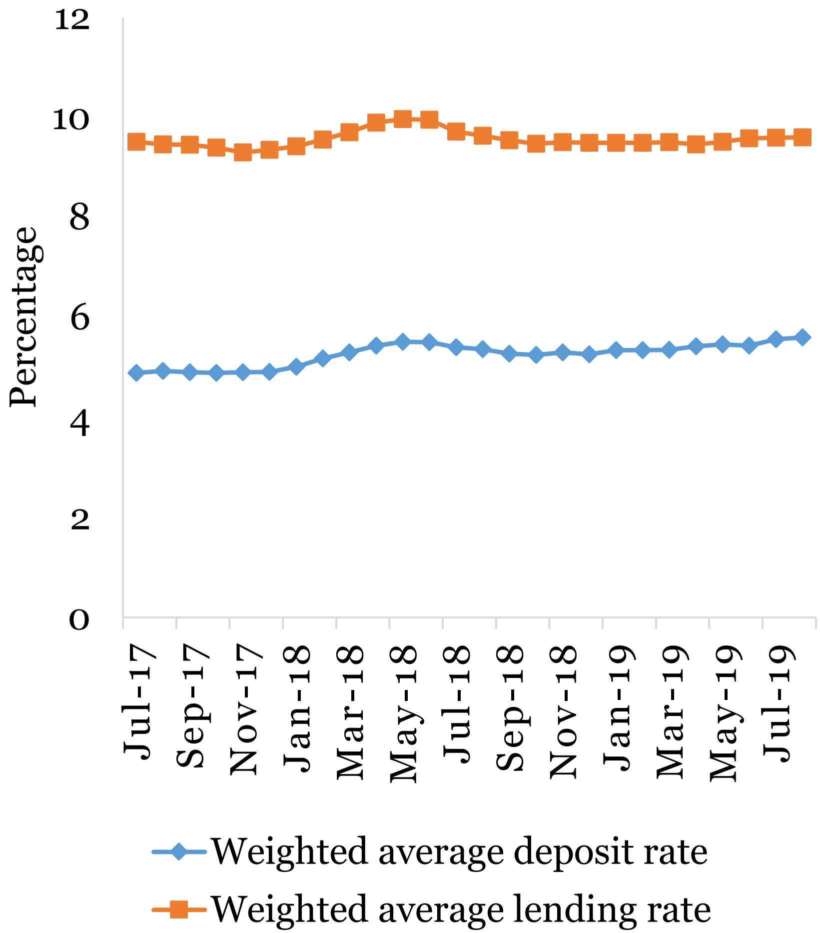
Figure: Change in liquid assets (in %)



Could cap on interest rate increase credit growth?

- Bangladesh Association of Bankers and Bangladesh Bank instructed banks to cap lending rates at 9% and deposit rates at 6%
- As of August 2019,
  - Weighted average deposit rate was 5.6%
  - Weighted average lending rate was 9.6%
- Since the weighted average deposit rate is very close to the point-to-point general CPI inflation rate, ***the real weighted average deposit rate* tends to hover around zero or slightly below zero**.
- CPD's earlier analysis has shown that proxy indicators of **private investment**, such as credit to the private sector, industrial term loan disbursement, import of capital machinery, and general index of manufacturing, have **no systematic relationship with lending rate**.
- Moreover, capping lending rates reduces access to finance for small and new businesses which have short credit histories, but which could otherwise have secured loans at higher lending rates.

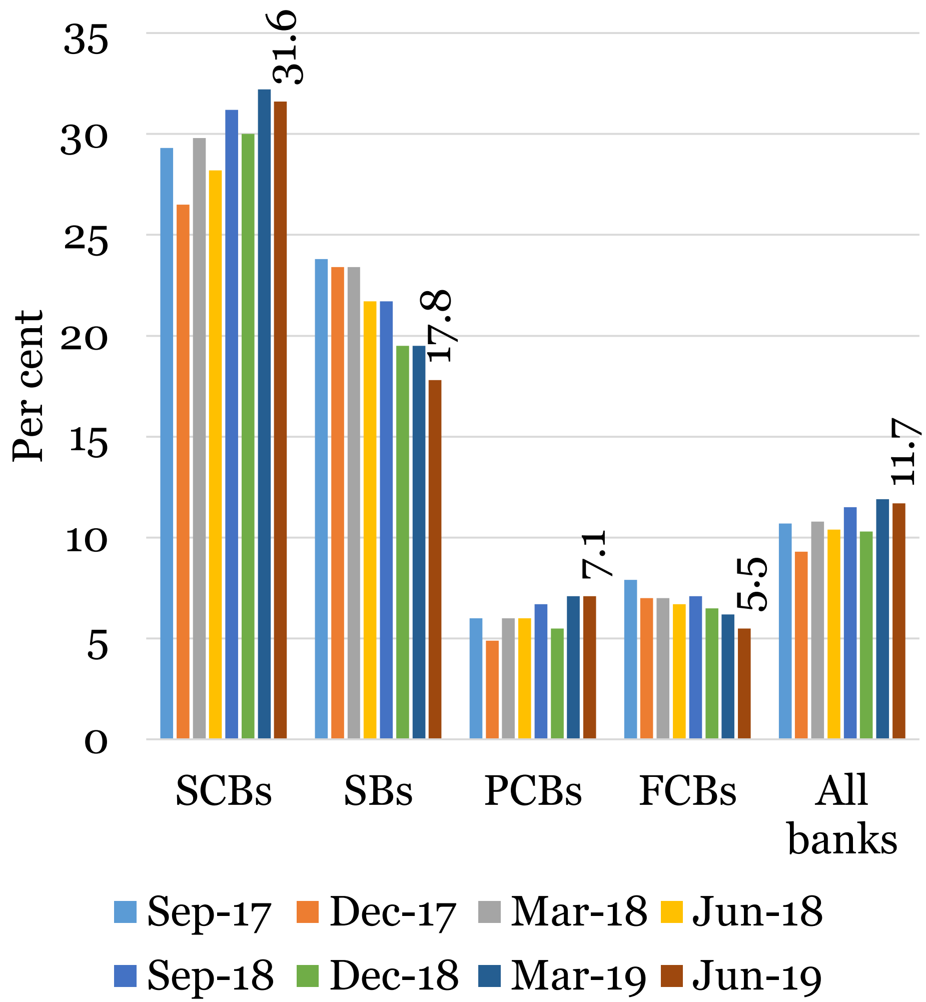
Figure: Weighted average interest rates in banks (in %)



Sky-rocketing NPLs affecting performance of banks

- NPL as a share of total outstanding loans increased from 10.41% in June 2018 to 11.69% in June 2019.
- **Total volume of NPL has increased from BDT 1,10,970 crore in March 2019 to BDT 1,12,430 crore in June 2019**.
- As of June 2019, both private commercial banks (PCBs) and foreign commercial banks (FCBs) had NPLs greater than 5% of total loans, while state-owned commercial banks (SCBs) had NPLs in excess of 30% of total loans.

Figure: Gross NPL as a share of total loans, by type of banks (in %)



Amount of NPL is greater than annual budget allocation for education and health combined!

Table: NPL compared to GDP and budget allocations for education and health sectors

FY	Amount of NPLs[i] (in billion BDT)	Gross NPL as % of total loans	NPL as % of GDP	Education budget as % of GDP	Health budget as % of GDP
2010	227	7.3	2.85	1.95	0.79
2011	226	6.1	2.47	2.01	0.80
2012	427	10.0	4.05	1.78	0.73
2013	406	8.9	3.39	1.73	0.71
2014	502	9.69	3.74	1.87	0.70
2015	594	8.79	3.92	1.85	0.69
2016	622	9.23	3.59	2.18	0.73
2017	742	9.31	3.76	2.19	0.34
2018	893	10.41	3.73	2.09	0.89
2019	**1124**	**11.70**	**4.43**	**2.10**	**0.90**

Source: CPD compilation from Bangladesh Bureau of Statistics (BBS), Bangladesh Bank Annual Report (various years), Budget documents (various years), Ministry of Finance (various years).

Note: i) NPL data is for calendar years; all other data are for fiscal years.

Outrageous opportunity cost of NPLs

❑What can Bangladesh do with **BDT 1,12,430 crores?**

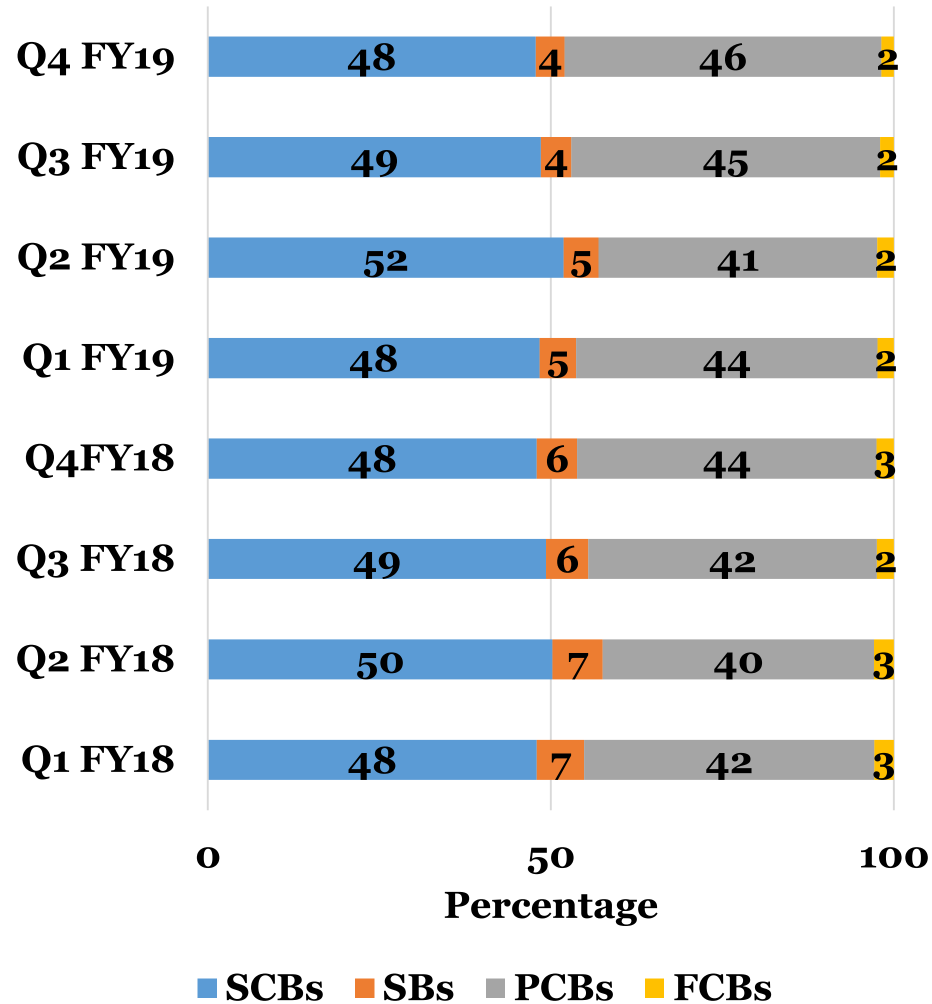
Total volume of NPLs in the banking sector was **BDT 1,12,430 crores** in June 2019	➔	**Build 3 road bridges** like the **Padma Multipurpose Bridge** (Cost: BDT 30,193 crores)
	➔	**Build 3 railway bridges** like the **Padma Bridge Rail Link** (Cost: BDT 34,988 crores)
	➔	**Build 3 powerplants** like **Matarbari** 2x600 MW Ultra-Super Critical Coal-Fired Power Project (Cost: BDT 35,984 crores)
	➔	**Build 5 metro rails** like the **Dhaka Mass Rapid Transit Development** Project (Metro Rail) (Cost: BDT 21,985 crores)
	➔	**Build 6 railway lines** like the Single Line Dual Gauge Track from **Dohazari-Ramu-Cox's Bazar and from Ramu to Ghundum** (Cost: BDT 18,034 crores)
	➔	**Build 7 powerplants** like 2x660 MW Moitree Super Thermal Power Plant (**Rampal**) (Cost: BDT 16,000 crores)

3. Banking Sector
Stuck in a Quagmire of Woes

PCBs also have high NPLs

- The distribution of NPLs in the banking sector during the period from Q1 FY18 to Q4 FY19 shows that:
    - SCBs' share of NPLs has been 49% on average
    - Specialised banks' (SBs) share of NPLs has fallen from 7% in Q1 FY18 to 4% in Q1 FY19
    - **PCBs' share of NPLs has risen from 42% in Q1 FY18 to 46% in Q4 FY19**
    - FCBs' share of NPLs has been 2% on average
- Such high concentration of NPLs in the PCBs reveals that **NPL is clearly not a problem affecting the SCBs only.**

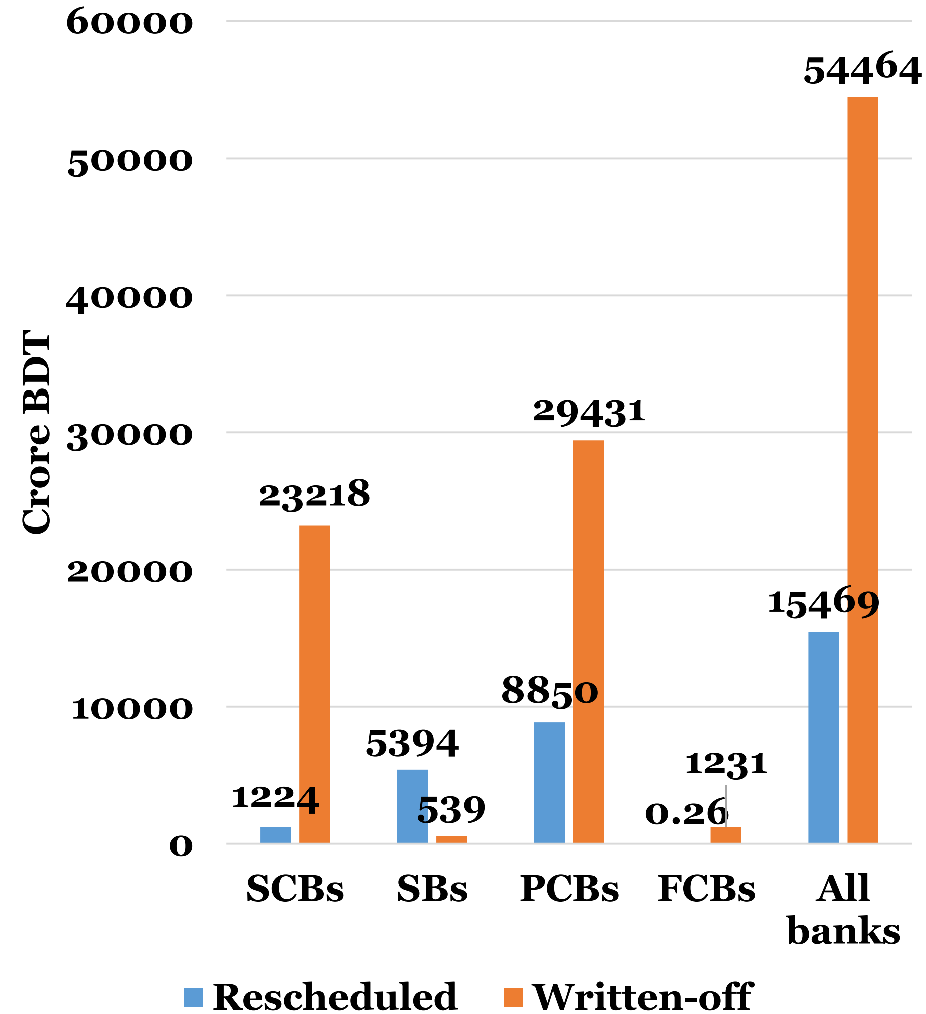
Figure: Distribution of NPL, by type of bank (as % of total NPL)



Massive rescheduling and writing-off, even by PCBs

- During the period April-June 2019, loans worth **BDT 15,469 crores** were **rescheduled**.
- As of June 2019, loans worth **BDT 54,464 crores** were **written off**.
- The PCBs had the highest proportion of rescheduled and written-off loans.
- If the **total amount of loans rescheduled and written-off** (BDT 69,933 crores) could be allocated for social protection, then the **annual budget of all social safety net programmes in Bangladesh** (except pension for government officials) could be **doubled**.

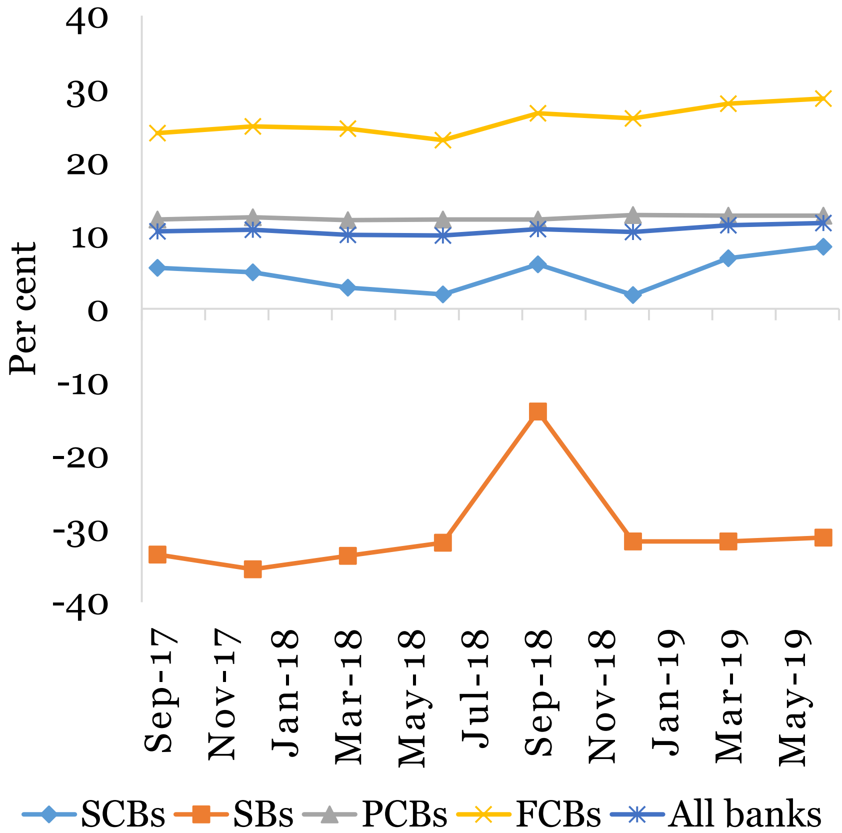
Figure: Rescheduled (April-June 2019) and written-off loans (as of June 2019), (in crore BDT)



Capital inadequacy of banks

- Bangladesh Bank's Guidelines on Risk Based Capital Adequacy state that banks in must maintain a minimum total capital ratio of 10% (or minimum total capital plus capital conservation buffer of 12.5%) by 2019, in line with BASEL III.
  - However, the SCBs have failed to maintain minimum requirements of capital adequacy.
  - On the other hand, the SBs have remained critically under-capitalised.
- **Without reducing NPLs, capital adequacy cannot be improved** since higher levels of NPLs lead to increased provisioning requirements, which results in capital shortfall.

Figure: Capital to risk weighted asset ratios, by type of banks (in %)



Rescuing banks through recapitalisation has been futile

- Recurrent recapitalisation of the SCBs by the government has emerged as an issue of grave concern, as the performance of the banks is not improving.
- It has been estimated that the government has spent **BDT 15,705 crore** in recapitalising the banks during the period FY2009-FY2017.
- This amount would be sufficient for building **4 deep sea ports like Payra**.
- The government had also come forward to rescue a PCB, The Farmers Bank Limited (now renamed as Padma Bank Limited), with a bailout package worth BDT 1,100 crore.
- This has set bad examples and will encourage banks involved in irregularities.

Privileges to promote perverse behavior of borrowers?

❑*Rebates*

Date and title	Measures taken	CPD's analysis
16 May 2019 BRPD Circular No. 04: Incentives to Good Borrowers	➢ Borrowers with no record of bad loan default in the last one year were offered a **10% rebate**	➢ Incentive for good borrowers is trivial compared to incentive provided to bad borrowers

Privileges to promote perverse behavior of borrowers?

❑*Down payment and repayment period*

Date and title	Measures taken	CPD's analysis
16 May 2019 BRPD Circular No. 05: Special Policy on Loan Rescheduling and One Time Exit	➢ Defaulters are allowed to pay only a **2% down payment** ➢ **10-year loan repayment period**, with a one-year grace period	➢ This will provide more incentive for defaulters to normalise bad debts ➢ Bad borrowers getting longer time to repay loans than good borrowers is surprising

Privileges to promote perverse behavior of borrowers?

❑*Interest rate*

Date and title	Measures taken	CPD's analysis
16 May 2019 BRPD Circular No. 05: Special Policy on Loan Rescheduling and One Time Exit	➢ Rescheduled loans would have to be repaid at only **9% interest rate**	➢ 9% interest rate falls within the lowest range of interest rates ➢ Those who had initially taken loans at a higher interest rates can now repay at a much lower rate; this may encourage borrowers to default

Privileges to promote perverse behavior of borrowers?

❑ *Waiver*

Date and title	Measures taken	CPD's analysis
16 May 2019 BRPD Circular No. 05: Special Policy on Loan Rescheduling and One Time Exit	➢ Central Bank has authorised banks to **waive all interest for defaulters**, depending on the bank-client relationship	➢ Measures such as these tend to legitimise corruption in banks by providing regulatory support

Privileges to promote perverse behavior of borrowers?

❑*One-time exit policy*

Date and title	**Measures taken**	**CPD's analysis**
16 May 2019 BRPD Circular No. 05: Special Policy on Loan Rescheduling and One Time Exit	➢ **'One Time Exit'** allows defaulters to pay the bare minimum, which includes bank's cost of funds and principal loan amount, with a condition of having to pay the outstanding amount within a year	➢ Such a general amnesty to loan defaulters cannot be justified on moral grounds ➢ Large defaulters of SCBs did not avail this policy ➢ PCBs, which account for almost half of all NPLs, were reluctant to offer such facilities

Privileges to promote perverse behavior of borrowers?

❑*End of repeatedly extended facilities?*

Date and title	Measures taken	CPD's analysis
23 October 2019 BRPD Circular Letter No. 23: Special Policy on Loan Rescheduling and One Time Exit	➢ **No more applications** from loan defaulters under the "Special Policy on Loan Rescheduling and One Time Exit", and applications submitted till 20 October 2019 will have to be settled by 19 November 2019 or the date fixed after disposal of the writ petition filed with the High Court	➢ Initially, defaulters were asked to apply within 90 days starting from 16 May 2019, but the central bank extended the time period two more times, which allowed even more loan defaulters to avail the facilities.

Privileges to promote perverse behavior of borrowers?

- These measures are completely **contradictory** to the broad **vision** of reducing NPLs that was mandated in the **election manifesto** (2018) of the ruling party. These are **likely to further aggravate the situation** of NPLs in the banking sector.
  - Such special privileges offered to loan defaulters may lead to a **moral hazard problem** since it could encourage all borrowers to take greater risks.

- In essence, it appears that the Central Bank has offered such privileges on the **premise that loan defaulters are mostly honest** and are genuinely finding it difficult to repay loans because of high interest rates.
  - Unfortunately, this **assumption is too simplistic and naïve** given the large number of willful defaulters.

Data availability: tightening the noose

- In recent months, **data** on the banking sector of Bangladesh have become **less accessible** and **less frequently available**.
- **Two annual reports and four quarterly reports are overdue:**
  - Report on banks and financial institutions for FY2018 (FID, MoF)
  - Report on banks and financial institutions for FY2019 (FID, MoF)
  - Bangladesh Bank Quarterly July-September 2019 (BB)
  - Financial Stability Assessment Report April-June 2019 (BB)
  - Scheduled Bank Statistics July-September 2019 (BB)
  - Non-Bank Financial Institutions (NBFI) Statistics April-June 2019 (BB)
- Four PCBs have failed to publish their mandatory disclosures as required under BASEL III.

Causes of the problems and the outlook

- The malaise of the banking sector is due to lack of governance and accountability ***mainly at four levels:***
  - *(i) Bangladesh Bank*
  - *(ii) Ministry of Finance*
  - *(iii) Commercial Banks*
  - *(iv) Judicial process*
- These problems suggest that an overall reform of the banking sector is urgently needed.

Causes of the problems and the outlook (contd…)

- ***(i) Bangladesh Bank:*** The **central bank** has **totally failed** to provide leadership in guiding commercial banks and financial institutions, and upholding its **sovereignty**. It has been cowed down not only by the **Ministry of Finance (MoF)**, but also by **influential individuals** having political connections. It should perform its duties in the following areas:
  - *The central bank should oblige all commercial banks to make their mandatory disclosures under BASEL III in a timely fashion.*
  - *Loans should be classified in accordance with international standards, such as those outlined by the International Monetary Fund's Financial Soundness Indicators guide.*
  - *Repeated rescheduling and writing-offs of NPLs should be stopped permanently.*
  - *Efforts should be made to recover NPLs through out-of-court procedures such as Alternate Dispute Resolution (ADR).*
  - *Single borrower exposure limit for commercial banks should be strictly enforced.*
  - *Loan defaulters should not be provided with more loans from the same bank or from other banks under any circumstances.*

Causes of the problems and the outlook (contd…)

- ***(ii) Ministry of Finance:*** The **Financial Institutions Division (FID)** of the MoF has been **disrupting the autonomy of Bangladesh Bank** in all major spheres.
  - *The MoF should not interfere in the autonomy of Bangladesh Bank, including in areas such as the appointment of Directors of Bank Boards, Managing Directors and Deputy Managing Directors of SCBs and the sanctioning of loans.*
  - *The report on banks and financial institutions for the fiscal years 2017-18 and 2018-19 should be published urgently by the FID in order to improve transparency.*

- ***(iii) Commercial Banks:*** **The owners of banks have also become the supervisors of banks.** As a result, bank management has lost its role, to a large extent, in improving the internal governance through skilled human resources, better risk management practices and strong internal control.
  - *Banking Companies Act should be amended to reduce both the number of family members in the board of directors and the tenure of each director.*

- ***(iv) Judicial process:*** **Lengthy disposal of loan default cases has created huge backlog in settlement of bank loans.** Therefore, banks cannot take actions against defaulters.
  - *The number of judges dealing with Money Loan Court Act 2003 and Bankruptcy Act 1997 ought to be increased.*
  - *Bankruptcy Act should be amended to remove mortgage-related loopholes that delay the course of justice.*

3. Banking Sector
Stuck in a Quagmire of Woes

Key messages

- The current ailing **banking system cannot sustain the ambition of high growth** in the country.

- **The severity of high NPLs is underestimated by the policymakers.**

- Increase in concentration of wealth and increase in volume of NPLs at the same time raise concerns regarding willful defaults of loans.

- At present, problems of the banking sector are being tackled by government's support. This is possible since banking assets are only about 56% of GDP. When banking assets will increase, the government may not be able to do so. In more developed economies, the share of banking assets in GDP is much higher. For example, in China it is 168%, in Malaysia 135%, and in Vietnam 130%.

- As Bangladesh prepares for graduation from a Least Developed Country (LDC) to a developing country and from a lower middle income country to an upper middle income country, it also has to develop a sound financial system which will ensure **finance for development, not finance for crony capitalism**.

- **Regrettably, the policymakers are stubbornly reluctant to comprehend the headwinds of the banking sector problems and take-up the required reform agenda.**

Section IV. Capital Market in Crisis

Market Volatility has aggravated further leading to Crisis Situation

- The volatility in the capital market has continued during the post-election period, and has increased further after the national budget announced in June, 2019 (level of volatility in Jul-Oct. period of 2018 and 2019: 100.5 vs. 163.3)
- **Low level of dividend offered by listed companies in FY2019**: Dividend increased for 9 cos; declined for 52 cos; no dividend offered by 23 cos (daily star, 30 Oct., 19)
- **Abnormal rise of prices of 'z' category shares**: Despite having any price sensitive information, prices of 'z' category shares have abnormally increased
- **Forced sales of shares by merchant banks:** The market experienced forced sales due to gradual decline in share prices

4. Capital Market in Crisis

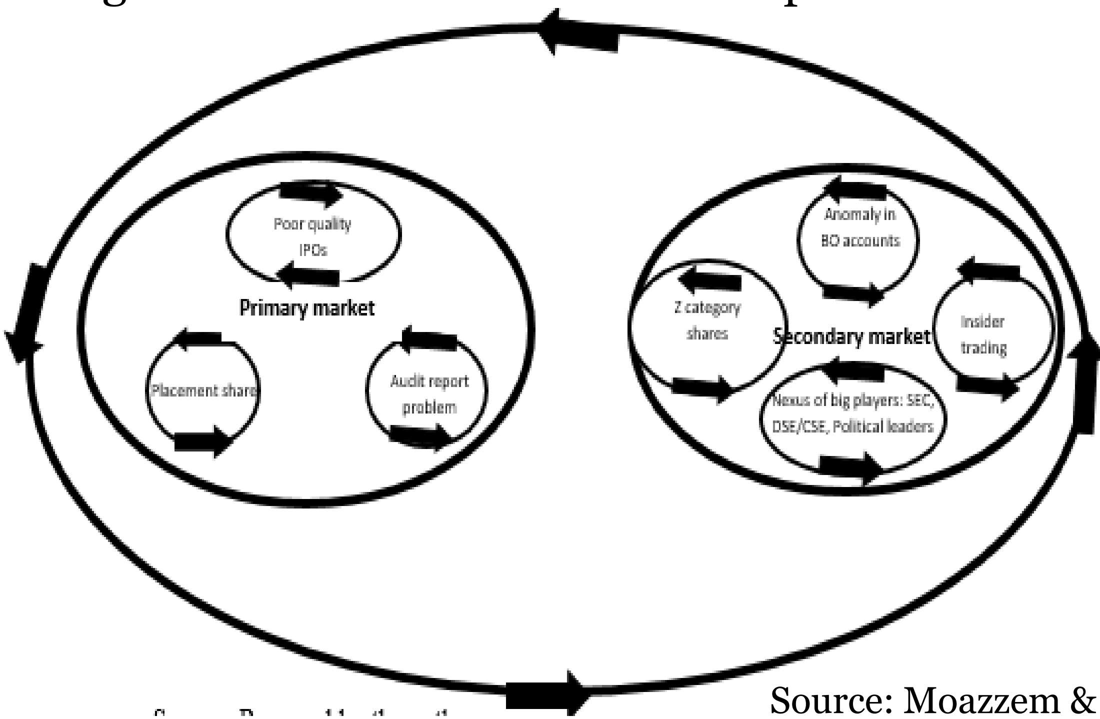
Market Volatility has aggravated further leading to Crisis Situation (Contd.)

- **Meager role of institutional investors:** Except few incidences, institutional investors are largely playing more or less a dormant role during this volatile period
- **Problems with major listed securities:** High NPL and problems in corporate governance have reduced confidence about shares of banks; GP's disputes with BTRC has an adverse impact on the market
- **No visible impact of strategic partnership with Chinese consortium:** No visible initiative has been undertaken by the Chinese consortium with regard to improvement of market surveillance and trading system, and introducing new products – as per commitment

Weak Institutions and Weak Governance are the Key Challenges

- CPD has repeatedly mentioned that weak institutions and weak governance are the major weaknesses of the market
  - Likewise pre-2010 period, a 'vicious cycle' of toxic elements' has been in operation in the market (Fig. 1)

Figure 1: Toxic Elements in the Capital Market



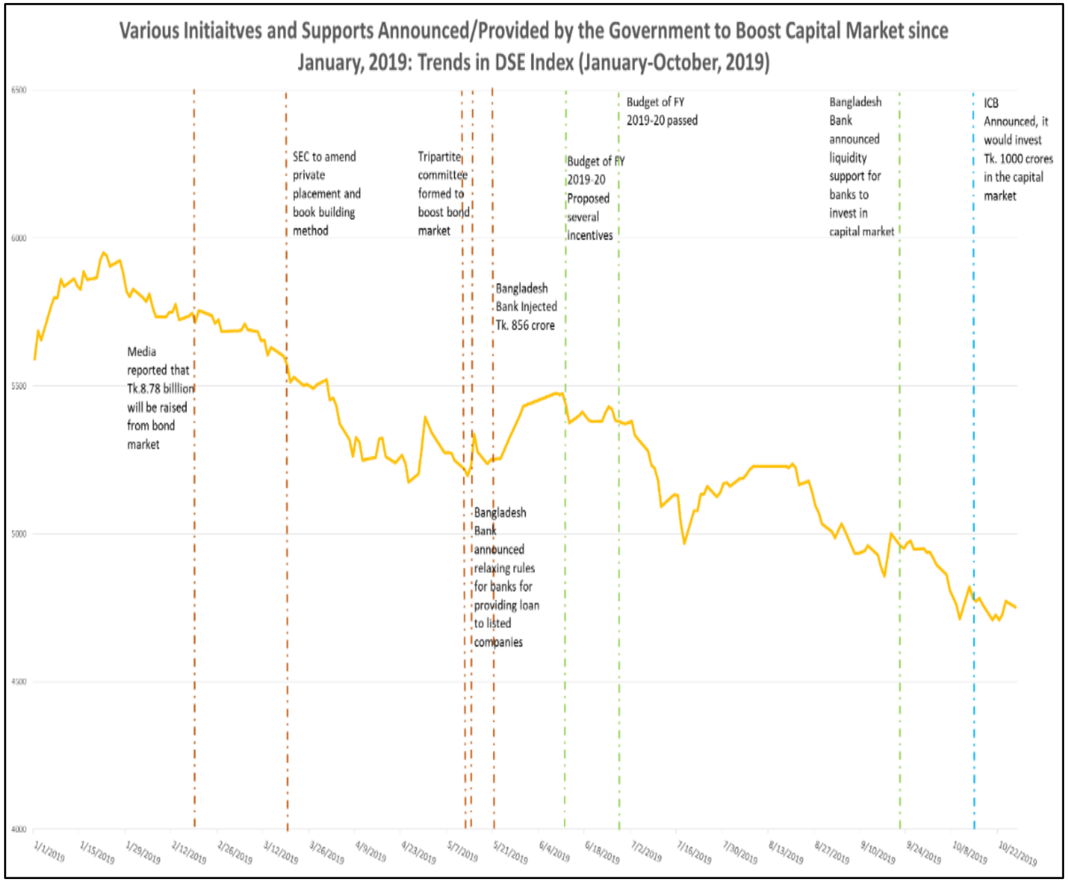
Source: Moazzem & Tariq, 2012

4. Capital Market in Crisis

Weak Institutions and Weak Governance are the Key Challenges (Contd.)

- The government has tried to address the challenges through a number fiscal and budgetary measures
  - Majority of the stakeholders have tendency to label the crisis from 'liquidity shortfall' point of view
  - Figure 2 shows that market did not respond to such measures as injection of capital undertaken since January, 2019

Figure 2: Non-response of the Market against Fiscal/Budgetary Measures



Source: Prepared by authors based on the data collected from the DSE Website

Weak Institutions and Bad Governance are the Key Challenges (Contd.)

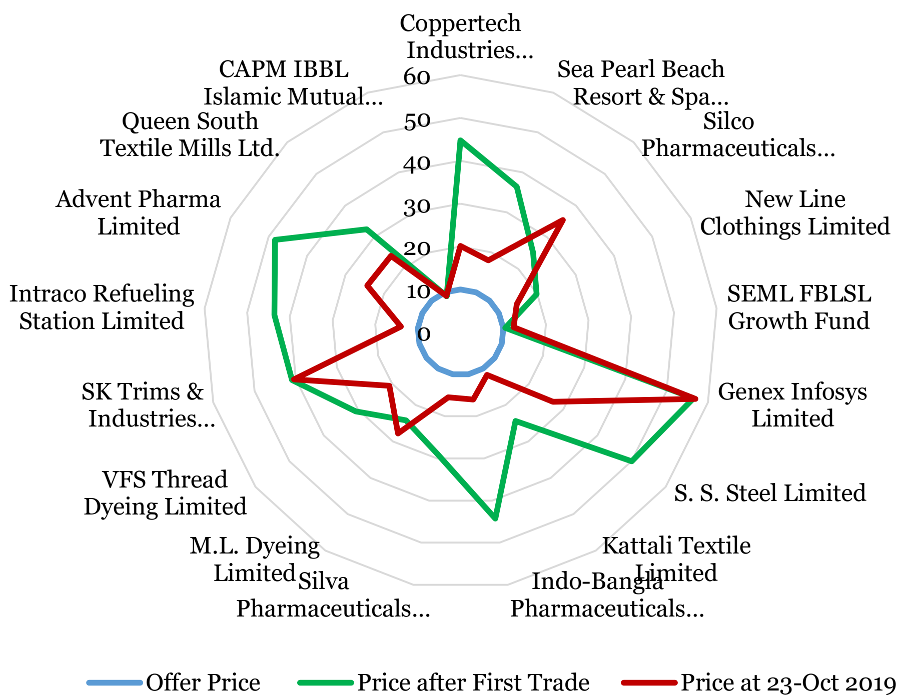
- CPD identified five institutional and governance related weaknesses concerning the market:
  - a) Poor quality IPOs
  - b) Anomalies in financial reporting
  - c) Lack of transparency in BO accounts
  - d) Suspicious trading in secondary market
  - e) Questionable role of institutional investors

4. Capital Market in Crisis

Poor Quality IPOs

- ❑ Most of these IPOs are considered to be of poor quality
  - ➢ Majority of shares lost their prices after few months; in certain cases, it has even declined below the initial offer price (Fig 3)
  - ➢ Questionable motive of company directors in raising fund, faulty financial reporting, non-compliance of issuers, lack of proper reviewing by DSE/CSE and lack of oversight by the SEC are responsible for such price movement
  - ➢ A total of seven IPOs have raised Tk.219 cr. during Jan-Oct., 2019 with an oversubscription of 305%

Figure 3: Trends in Share Prices of Newly Listed Secutries of 2018 and 2019



Source: DSE Website, 2019

- ❑ **Outlook:** IPO review process needs to be streamlined and made more stringent
  - ➢ Unlike other countries (India, USA), no specific punishment is mentioned for IPO related irregularities in BSEC Ordinance

Anomalies in Financial Reporting

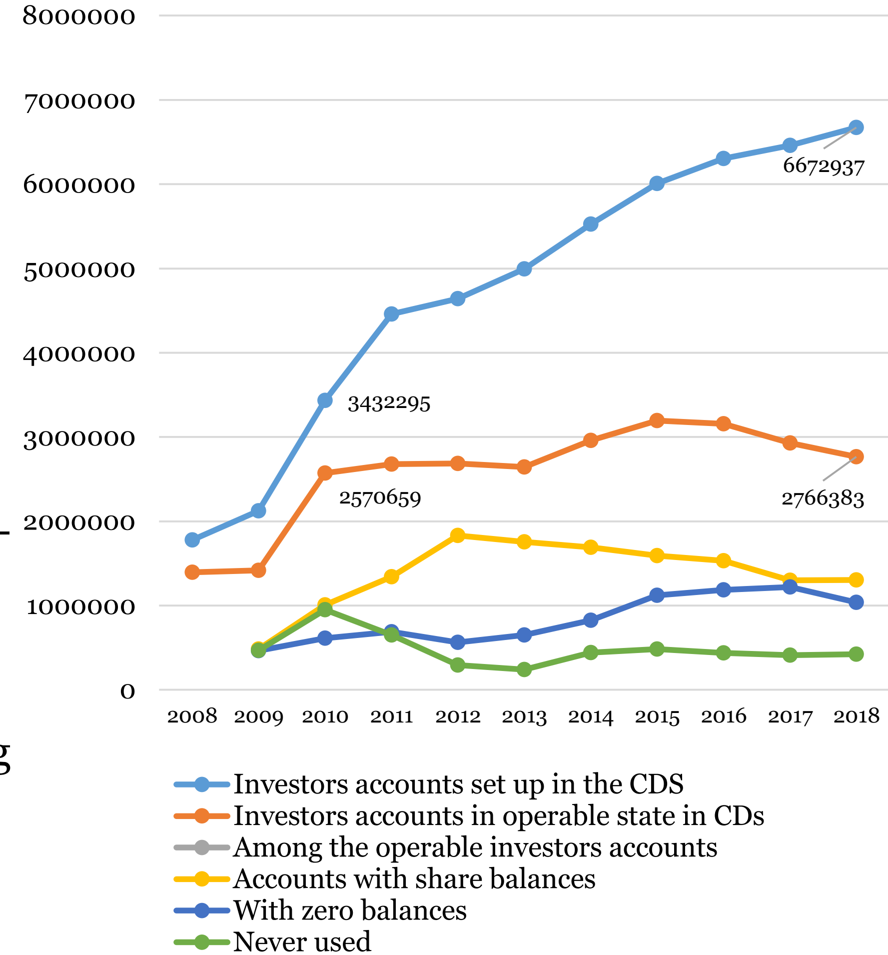
- The market has been suffering from poor quality of financial reporting of listed companies and of new IPOs
  - There are allegations against number of audit firms listed in BSEC's panel of auditors
  - BSEC revised the panel in July, 2019 only by dropping one auditor and retaining the rest 39 firms
- Lack of due diligence of respective agencies is a major concern: BSEC, FRC, ICAB and DSE/CSE
- **Outlook:** All financial reports must be vetted by a third party: FRC should play that role

4. Capital Market in Crisis

Lack of Transparency in BO Accounts

- Lack of transparency of BO account holders is a major weakness
  - Various types of malpractices could take place using BO accounts
- Since the crisis in 2010, number of investors accounts in operable state did not change in a tangible way (from 25.7 lac to 27.7 lac in 2018)
  - Curiously, number of investors account registered in CDS increased astronomically – from 34.3 lac in 2010 to 66.7 lac in 2018 – the question is who are these account holders?
  - Why the gap between account holders and operable account holders has been widening significantly over the recent past years?
  - Despite no major change in operable investment accounts, how these new accounts have been used by the account holders?

Figure 4: Investors Accounts in the CDS: Who Are Those?



Source: CDBL, Different Annual Reports

Lack of Transparency in BO Accounts (Contd.)

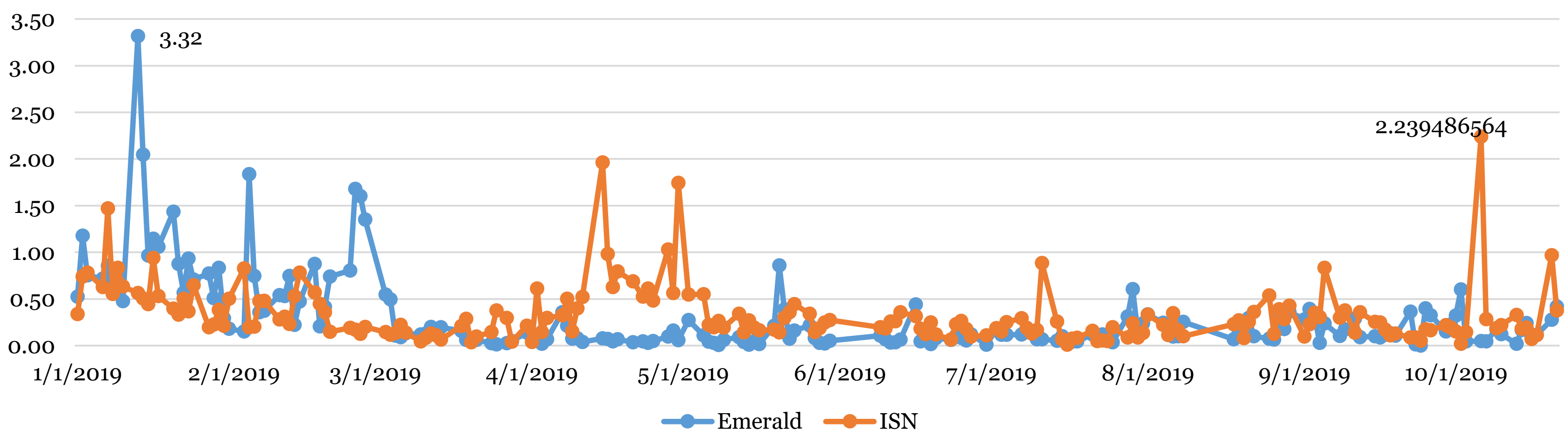
- Are the concerned authorities doing due diligence in this regard?
    - CDBL, brokerage houses, DSE/CSE and SEC
- **Outlook:** Existing system of opening BO account needs to be revised
    - It is important to make presentation of TIN certificate mandatory along with bank certificate and NID for existing and new BO accounts
    - Identity of BO account holders needs to be made public through CDBL website

4. Capital Market in Crisis

Suspicious Trading in the Secondary Market

- **Trading of 'Z' Category Shares:** It is alleged that a group of BO account holders used low-cap companies (z categories) and artificially raised their prices through serial trading
  - Unfortunately BSEC and DSE/CSE's upgraded surveillance software could not properly identify such trading malpractices
- Z category shares are often found in top-gainers' list of the DSE (On 30 October, 61.2% of Z category shares have gained while A' category shares gained by 54.8%)
  - Daily trading pattern of two selected z category securities went up to as high as 2.2% to 3.3% of their total shares (Fig. 5)

Figure 5: Daily Trading Pattern of Two Z Category Shares



Source: Prepared by authors based on the data collected from the DSE Website

4. Capital Market in Crisis

Suspicious Trading in the Secondary Market (Contd.)

- **Insider Trading:** Despite allegations of insider trading at the company level, SEC has taken action against directors of only a few companies
- **Illegal Activities of Brokerage Houses:** Several brokerage houses are alleged to have been involved in illegal activities using private BO account holders
  - SEC identified a few and took punitive measures but same others are still in operation
- **Outlook:** Transparency in trading by taking action against those operating multiple BO accounts and real-time monitoring and surveillance of BO accounts need to be ensured
  - Chinese strategic partner should make the required investment for strengthening market surveillance as per commitment
  - CDBL should play its role in sharing timely information with the BSEC to help take necessary measures
  - Stern measures are needed against those involved in insider trading and the brokerage houses involved in illegal activities

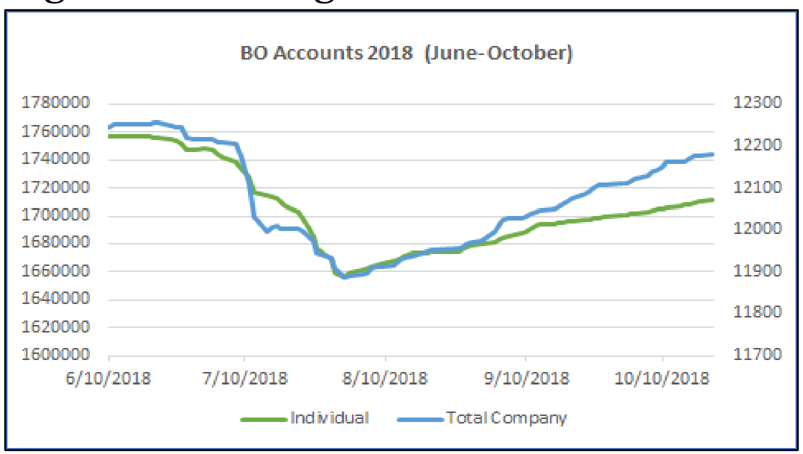
Questionable Role of Institutional Investors

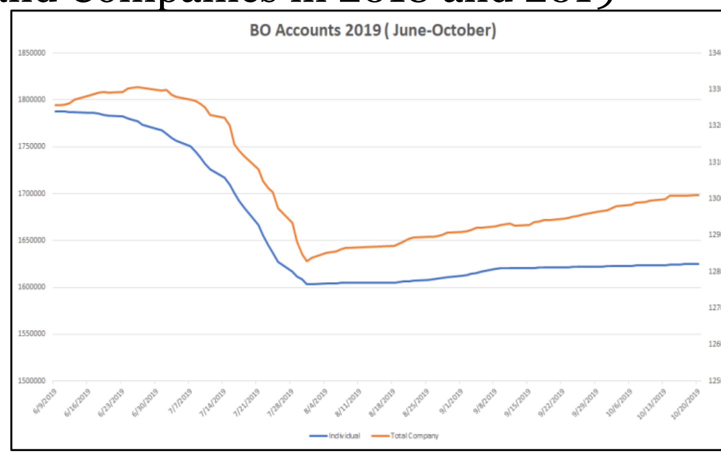
- Institutional investors have failed to play their due role in stabilising the market. Rather they are to some extent contributing to destabilisation of the market
- About 60% of market shares are in the hand of a limited no. of investors
    - 40% owned by 1100 eligible investors, 10% by 37 mutual funds, and 10% by 22000 NRBs. Pattern of distribution of shares at pre-IPO stage contributes to it
    - In contrast, 3 million BO account holders own 40% of total market shares

Questionable Role of Institutional Investors

- ❑ Analysis of trading behaviour of individual and company account holders reveal no significant difference between the two players (Figure 6)
  - ➢ More importantly, institutional investors are found to behave more in ‘herd-like’ manner compared to individual account holders

Figure 6: Trading Behaviour of Individual and Companies in 2018 and 2019





Source: Prepared by authors based on the data collected from the CDBL Website

- ❑ **Outlook:** Necessary guidelines need to be prepared for institutional investors in order to improve their trading practices in the market
  - ➢ For example, India has specific guideline for foreign institutional investors

The Capital Market Is Yet to Become an Alternate Source for Investors

- The market is yet to emerge as an effective alternate source for raising funds by private companies
  - Efforts to develop equity market in parallel with debt market has failed time and again
    - A key reason is lack of market confidence among investors owing to lax monitoring and enforcement of rules and regulations by the involved public and private agencies
- Market irregularities and malpractices have created scope for 'siphoning off' large amount of funds by a section of influential quarters/vested groups
  - As a result, small investors have been betrayed time and again, and have lost their hard-earned savings by participating in so-called 'elusive market'

4. Capital Market in Crisis

The Capital Market Is Yet to Become an Alternate Source for Investors (Contd.)

- Government and other stakeholders need to come out from the so called narrative of 'fund crisis' which is often demanded by the vested quarters for injection of new funds
  - Proposed 'bond market' should be developed with due caution, taking into cognisance the weak monitoring and enforcement system to tackle possible market irregularities
- SEC's leadership needs to be strengthened. SEC's operational independence needs to be ensured in case of surveillance, market monitoring and enforcement of rules and regulations
  - Other public and private agencies such as FRC, DSE/CSE, CDBL, ICAB and institutional investors need to play their due role and should coordinate their activities

Section V. External Sector Performance

The Gathering Cloud

5. External Sector Performance
The Gathering Cloud

Overall BoP Position: Disquieting Trends on Several Counts

Table: Balance of Payments (Million USD)

Items	Actual		7FYP Projection		Actual	
	FY18	FY19	FY19	FY20	Jul-Aug FY19	Jul-Aug FY20^{P}
Trade Balance	-18179	-15494	-16490	-18670	-2107	-1975
Export f.o.b. (including EPZ)	36285	39945	47462	54106	6718	6647
Import f.o.b. (including EPZ)	54463	55439	63952	72776	8825	8622
Services	-4201	-3715	-7672	-8746	-384	-510
Primary Income	-2641	-2930	-6374	-7561	-285	-323
Secondary Income	15453	16885			2769	3121
Of Which: Workers' remittance inflow	14703	16196	23085	25393	2729	3042
Current Account Balance	-9567	-5254	-6351	-8284	-7	313
Capital Account	331	233	850	900	3	4
Financial Account	9011	5628	10960	13703	521	164
Of which: FDI (gross)	3290	4501	7440	9993	688	737
Overall Balance	-857	12	5459	6318	156	139

5. External Sector Performance
The Gathering Cloud

- For the first time since FY11, the overall balance was negative in FY18 [USD (-)857.0 million]. In FY19 it barely made into the positive terrain [USD (+)12.0 million). For the first two months of FY20, the balance was (USD 139.0 million) - lower than the corresponding balance for FY19 (USD 156.0 million)
- The gap between actual performance and 7FYP projections as regards BoP elements has been on the rise – this concerns all the four elements:
  - Trade balance;
  - Current account balance;
  - Capital account; and
  - Financial account
- The early signals in FY20 also indicate continuation of these recent trends
- If this trend continues over the rest period of FY20, the overall balance, forex resources, exchange rate will come under increasing pressure
- In view of this, maintaining competitive exchange rate, reversing the negative export trend and ensuring robust flow of remittances and replenishing the forex resources will be required to maintain robust BoP and ensure overall macroeconomic stability

5. External Sector Performance
The Gathering Cloud

Export Performance

- **For the first time since FY10 the growth of exports in the first quarter has been negative in FY20**

Table: Export Growth in July-September, FY20		
	FY20 (Q1)	Required Growth Rate to reach target FY20 (Q2-Q4)
RMG	-1.6 %	16.2 %
Non-RMG	- 9.1 %	22.8 %
Total	-2.9 %	17.2 %
Source: Computed from EPB		

- The higher deceleration in non-RMG exports is indicative of growing export concentration in RMG, undermining the target of export diversification
- If the export target of FY20, at 12.3%, is to be attained, exports will need to register a robust growth of 17.2% over the next 3 quarters compared to corresponding period of FY19

The outlook for FY20 is rather bleak with consequent implications for external sector performance. IMF's global growth projection lowest since 2009

- Global economic outlook: Both the IMF and the World Bank have reduced global growth projections. IMF's growth projections for 2019, at 3.0 per cent, is lower than actual global growth rate achieved since the financial crisis of 2007-08

Table : Global Growth Projections

	2019	2020	2021	2024
IMF: April, 2019	3.3	3.6	-	3.7
: October, 2019	3.0	3.4	-	3.6
World Bank: January, 2019	2.9	2.8	2.8	-
: June, 2019	2.6	2.7	2.8	-

Source: IMF, World Bank: Global Economic Prospects

5. External Sector Performance
The Gathering Cloud

- Declining share in US market; lack of market diversification: Bangladesh is falling behind its major competitors in the key market of the USA. Bangladesh's export growth in USA over first two months was 3.1%. In contrast: Cambodia (8.2%); China (4.9%); Turkey (10.3%); Vietnam (11.7%)
- In the EU market the performance was better, with growth of 4.9%which matched that of Vietnam
- However, in non-traditional (non-USA, non-EU) markets the growth rate has been quite discouraging, at (-) 11.1%
- In recent past years there has also been a fall in RMG prices
- The trends indicate that the target of market diversification is not being attained. Thus,
  - One conclusion that can be drawn is that the policy of cash incentives being pursued by Bangladesh, without adequately addressing the underlying factors of export competitiveness and conducive business environment, is not giving the expected results
  - Incentives are no substitute for addressing underlying factors that undermine competitiveness

Fiscal incentives for export need revisiting

- In FY20, allocation for fiscal incentives for export was USD 470.0 million, with USD 360.0 million added on for remittance (2% each incentives)
- As Bangladesh moves towards LDC graduation, such cash incentives may come under closer scrutiny
- What is also becoming increasingly apparent, based on export performance, is that without addressing the underlying factors of competitiveness, incentives alone will not serve the purpose
- In surveys carried out by the CPD for the GCR, as also borne out by other surveys, entrepreneurs and exporters prioritise the followings:
  - Quality infrastructure
  - Enhanced ease of doing business
  - Access to finance at competitive price
- There is a need to revisit the relative efficacy of incentives and raise allocative efficiency by focusing on the identified priorities

5. External Sector Performance
The Gathering Cloud

Exchange Rate Management

- **CPD-IRBD proposition of gradual depreciation of currency still holds**
- Exchange rate management has emerged as an important factor in Bangladesh's external sector performance
- Earlier, in successive IRBDs CPD had proposed that Bangladesh should pursue a policy of gradual depreciation in view of the exchange rate movement of currencies of key competitors and taking into cognisance the interests of external sector
- The relative movement of BDT with competing currencies indicates that majority of other currencies have been depreciating at faster pace during Jan-Sep 2019 period (not to speak of earlier significant depreciation of compelling currencies)

Table: Currency movement of selected countries (January to September 2019; Base January 2019 = 100)

Time	Bangladesh	Cambodia	China	India	Pakistan	Turkey	Vietnam
Jan-19	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Sep-19	100.7	102.1	104.8	100.8	112.6	106.4	101.3

Source: CEIC Data

5. External Sector Performance
The Gathering Cloud

- During January-October 2019 the difference between official exchange rate of BDT and the curb market rate (vis-à-vis USD) has been on the rise indicating need for currency adjustment in an ongoing basis

Table: Official Exchange Rate and Curb Market Rate

Date		29-Jan	27-Feb	31-Mar	30-Apr	30-May	30-Jun	30-Jul	29-Aug	30-Sep	29-Oct
USD Selling Rate	Official	83.95	84.15	84.25	84.45	84.50	84.50	84.50	84.50	84.50	84.75
	Curb	84.5	84.5	85.2	85.3	85.5	85.2	85.5	86.5	87.5	86.4
Difference (%)		0.7	0.4	1.1	1.0	1.2	0.8	1.2	2.4	3.6	1.9

Source: Bangladesh Bank and Market Information

- This underscores the need for strategic exchange rate management in view of the emerging scenario concerning the external sector

Remittance Flows

- **The silver lining is remittance growth, but uncertainties remain because of increasing volatility of recent times**
- The BoP position would have deteriorated further had not the remittance flow picked up in FY18 and FY19 (17.3% and 9.6% growth respectively) following negative growth of (-)14.6% in FY17
- In Q1 of FY20 remittance growth was a robust 16.6%
- However, there has been a significant fall in number of workers leaving: Following 10.08 lac in 2017 and 7.34 lac in 2018, over the first 9 months the number of workers leaving was 4.7 lac indicating that the number will be less than in 2018
- Remittance flow is experiencing significant volatility in recent years: between FY01 and FY13, there has been persistent positive growth in remittance earnings, over the FY14-FY19 period, there was negative growth for three years
- The scenario of migrant labour market is undergoing significant challenges
  - Needed more energetic exploration particularly in regional markets (South Korea, Malaysia and Japan)

Forex Reserves

- **Declining forex reserve will constrain capacity of the central bank in trade and exchange rate management**
- The forex reserves, following rapid rise between FY11 and FY17 has been stagnating since. Indeed, in FY20 (September) it has come down by about 0.9 billion US$ compared to the corresponding time of FY19.
  - From earlier 8.5 months of import equivalent to 4.5 months of import equivalent

Year	Reserve	Import Equivalent (Month)
FY 2010-11	10911.6	3.7
FY 2011-12	10364.4	3.2
FY 2012-13	15315.2	4.6
FY 2013-14	21558.0	5.9
FY 2014-15	25025.2	6.7
FY 2015-16	30168.2	7.8
FY 2016-17	33493.0	8.0
FY 2017-18	32943.5	6.0
FY 2018-19	32716.5	5.5
FY 2019-20*	31831.9	4.5
*End of September 2019		

5. External Sector Performance
The Gathering Cloud

Key Messages

- ❑Pursue policy of gradual depreciation of the BDT
- ❑Recalibrate fiscal support to address underlying factors of competitiveness rather than relying only on cash incentives
- ❑Take adequate preparation to remain competitive following LDC graduation: preference erosion; change in rules of origin
- ❑Take measures to improve BoP position by particularly focusing on improving current and financial account balances

Section VI. Concluding Observations

6. Concluding Observations

Highlights

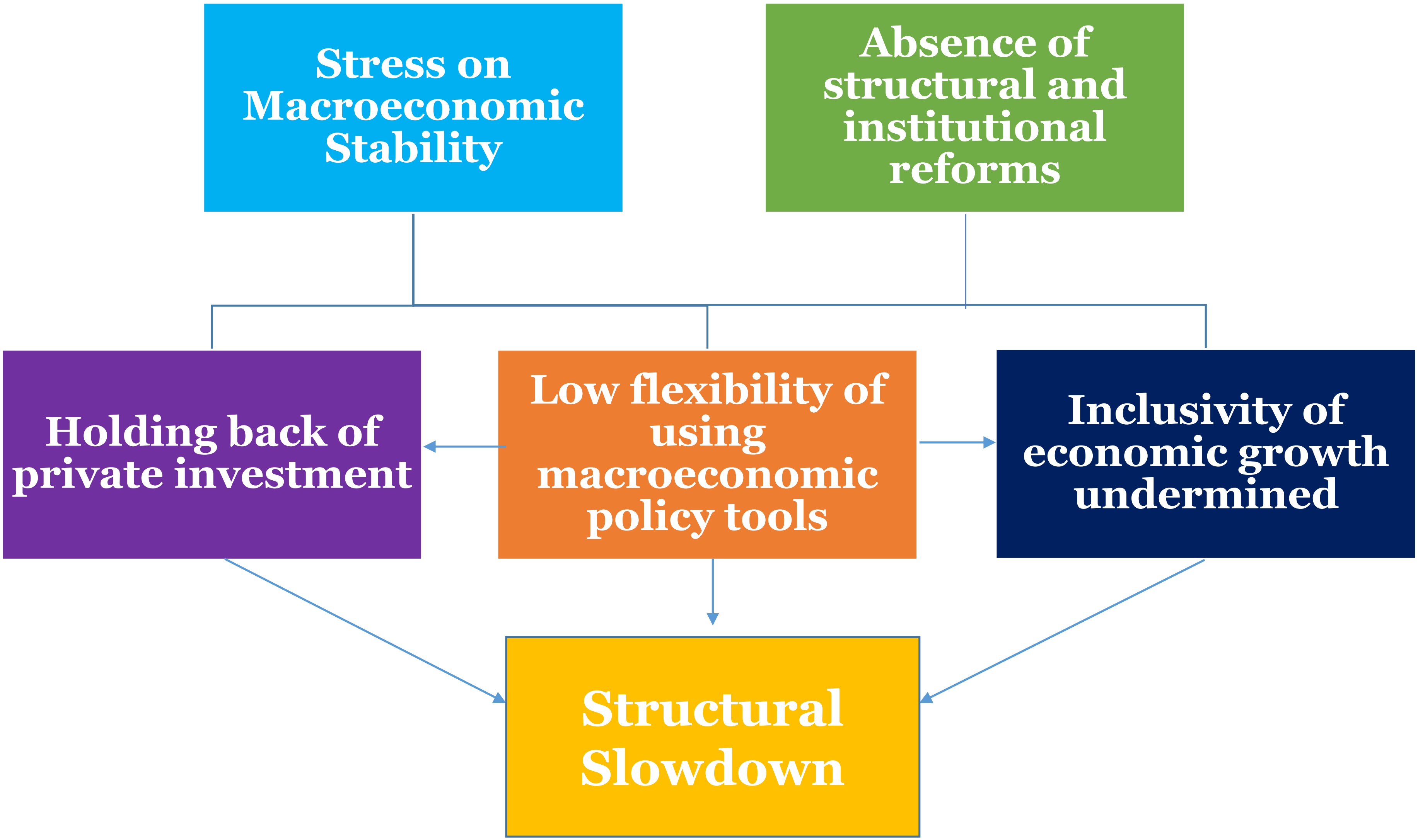
- There is a growing stress in the macroeconomic stability
- Overall situation aggravated as very little structural and institutional reforms are undertaken in the economy
- This has also diminished the scope to use macroeconomic policy tools; lesser flexibility

6. Concluding Observations

Implications

- **Lack of structural and institutional reforms is holding back <u>private investment</u>**
- **These are impacting on mid-term drivers of growth i.e. <u>human capital/resource</u>**
- **<u>Inclusivity</u> of economic growth is also affected**
- **All these may lead to <u>structural slowdown</u> which will undermine sustainability of the economic growth**

6. Concluding Observations



Independent Review of Bangladesh's Development

Thank You